80-655

No.

Supreme Court, U. S.
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In the

Supreme Court of the United States

NICHOLAS J. NICKOLAOU and
AUDREY LOMBARDI,

Petitioners,

vs.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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QUESTION PRESENTED

What is the burden of proof in hearings before the Commission and the CBOE?

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IN THE

SUPREME COURT OF THE UNITED STATES

No.

NICHOLAS J. NICKOLAOU and
AUDREY LOMBARDI,

Petitioners,

vs.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

Petitioners Nickolas J. Nickolaou ("Nickolaou"), and Audrey Lombardi ("Lombardi") respectfully pray that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals affirming the order and decision of the Securities and Exchange Commission (the "Commission") which affirmed, in part, the order of the CBOE.

The orders of the Commission and the United States Court of Appeals affirming the Commission are included in the Appendix.

JURISDICTIONAL STATEMENT

The jurisdiction of this Court is invoked pursuant to 28 U.S.C. §1254(1).

QUESTION PRESENTED

What is the burden of proof in hearings before the Commission and the CBOE?

ARGUMENT

THE BURDEN OF PROOF REQUIRED of the CHICAGO BOARD OF OPTIONS EXCHANGE, INC. ("CBOE") and of the SECURITIES AND EXCHANGE COMMISSION ("the Commission") in these proceedings is the CLEAR AND CONVINCING STANDARD OF PROOF.

The Court has granted certiorari in a companion case regarding the same issue. *Steadman* v. *Securities and Exchange Commission,* 603 F. 2d 1126 (5th Cir., 1979) cert. granted (DKT 79-1266) 48 U.S.L.W. 3698 (April 28, 1980). The issue in that case is controlling on the question presented in the instant case.

CONCLUSION

For the foregoing reasons this Court should grant certiorari and the Writ of Certiorari issue forthwith.

Respectfully submitted,

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APPENDIX

UNITED STATES COURT OF APPEALS

For the Seventh Circuit

Chicago, Illinois 60604

July 18, 1980

(Argued April 29, 1980)

Before

Hon. THOMAS E. FAIRCHILD, *Chief Circuit Judge*
Hon. WALTER J. CUMMINGS, *Circuit Judge*
Hon. ROBERT A. GRANT, *Senior District Judge*•

NICHOLAS J. NICKOLAOU and
AUDREY LOMBARDI,

Petitioners,

vs.

No. 79-2314

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

Petition for Review of an Order of the Securities and Exchange Commission.

ORDER

This case involves an attempt to fraudulently depress the market price of common stock of the International Business Machines Corporation ("IBM") to financially benefit a member of the Chicago Board Options Exchange, Inc., ("CBOE"), all in violation of rules of the CBOE.

Nicholas J. Nickolaou, a member of the CBOE, and Audrey Lombardi, an employee in the Chicago office of

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• Senior District Judge Robert A. Grant of the Northern District of Indiana is sitting by designation.

Merrill Lynch, Pierce, Fenner and Smith, a CBOE member firm, have petitioned this court pursuant to Section 25(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78y(a), for review of an order of the Securities Exchange Commission ("Commission") affirming the disciplinary action taken against petitioners by the CBOE.

The underlying facts are that at the close of trading on March 29, 1977, Mr. Nickolaou was short 39 IBM April 280 call options which, in layman's language, means that he had written 39 call options, each of which granted the holder the right to purchase 100 shares of IBM stock at a price of $280 per share on or before the Saturday immediately following the third Friday in April 1977. On the following day, March 30, 1977, the price of IBM stock on the New York Stock Exchange opened at $280½ per share. Within a ten-minute period that morning, Merrill Lynch's Chicago wire room, which telephonically connects the Chicago office with Merrill Lynch brokers on the floor of the New York Stock Exchange, received three forged order tickets which purportedly authorized the sale of 37,000 shares of IBM common stock at market price for the account of a Merrill Lynch customer, Combined Insurance Company. The order tickets were delievered to the wire room by means of a pneumatic tube connecting the wire room with Merrill Lynch's Institutional Department. The tickets showed a customer account number (subsequently found to be inactive) and the identification number of a Merrill Lynch account executive, as well as unsual typographical errors. The information on the tickets was sufficiently complete so that the orders could have been transmitted to the floor of the New York Stock Exchange for execution. However, a wire room employee questioned the tickets because they were not filled out correctly and stopped their transmission. Neither the account executive whose identification number was on the tickets nor any other person in the institutional Department, including Ms. Lombardi, admitted any knowledge of the order.

Ms. Lombardi was a friend of Mr. Nickolaou's and in an application to the CBOE for a floor badge, he had designated her as an employee. Although he had no official business with the Institutional Department of Merrill Lynch's Chicago office, Mr. Nickolaou frequented that department in the morning and in the afternoon, waiting to pick up Ms. Lombardi. His presence in Ms. Lombardo's work area was considered inappropriate by the manager of the Institutional Department.

On January 6, 1978, the Business Conduct Committee of the CBOE ordered disciplinary proceedings against Mr. Nickolaou and Ms. Lombardi, having concluded that there was probable cause for finding a violation of the Exchange's rules. The charges alleged that Mr. Nickolaou prepared and delivered to Merrill Lynch, in concert with Ms. Lombardi, the three fictitious market order tickets to sell a total of 37,500 shares of IBM common stock for execution on the New York Stock Exchange. The charges alleged that Ms. Lombardi received the three fictitious order tickets from Mr. Nickolaou, and caused them to be placed in the Merrill Lynch pneumatic tube system for execution on the New York Stock Exchange. This conduct by Mr. Nickolaou and Ms. Lombardi was alleged to be in violation of CBOE Rules 4.1 and 4.2 prohibiting conduct inconsistent with just and equitable principles of trade. The charges also alleged that Mr. Nickolaou and Ms. Lombardi violated CBOE Rules 4.2 and 4.7 by engaging in this conduct for a manipulative purpose. An evidentiary hearing, at which the petitioners were represented by counsel, was held in April 1978 before the Business Conduct Committee. The staff of the CBOE presented documentary and testimonial evidence against the petitioners and counsel for petitioners cross-examined the CBOE staff's witnesses. A handwriting expert testified that he had compared the handwriting on the order tickets with the handwriting on 35 of Mr. Nickolaou's own trading cards, with his membership application, and with other handwriting materials in his CBOE membership file. Most of those

examplars were acknowledged by Mr. Nickolaou to be his handwriting. The expert, based on his comparison, concluded that the same person who had filled out the exemplars had filled out the forged tickets. At the conclusion of the CBOE staff's presentation, petitioners moved to dismiss the charges on the ground of insubstantial evidence. The Business Conduct Committee denied the motion. Despite specific and repeated requests by the panel of the Business Conduct Committee that petitioners testify, both petitioners refused to do so.

In a decision dated June 22, 1978, the CBOE Business Conduct Committee concluded that petitioners had violated the rules as charged. The Committee found that both petitioners' failure to testify and answer the Committee's questions gave rise to an inference that their testimony would have been adverse. Noting that the placing of fictitious orders may cause unwarranted losses to participants both in the stock and options markets, the Committee determined to impose a sanction on Mr. Nickolaou consisting of a three-year suspension from Exchange membership and association with an Exchange member, a $10,000 fine, and a censure. The Committee concluded that, based upon Ms. Lombardi's subsidiary role in the scheme, imposition upon her of a censure was a sufficient sanction.

Mr. Nickolaou and Ms. Lombardi petitioned the Board of Directors of the CBOE for review of the Business Conduct Committee's decision, pursuant to CBOE Rule 17.9(a). In a decision dated September 13, 1978, the Board rejected petitioners' argument that the Committee's decision was contrary to the weight of the evidence and also rejected certain procedural exceptions to the Business Conduct Committee's decision raised by petitioners. The Board concluded that the manipulative scheme in which petitioners had been found to have engaged was calculated to depress the market price of IBM stock so that Mr. Nickolaou could profit from his short position in IBM call option contracts, and that this course of conduct exhibited a blatant disregard for the interests

of the investing public and the Exchange. On its own motion, the Board increased the sanction imposed on Mr. Nickolaou to expulsion from Exchange membership and affirmed the censure and fine imposed on Mr. Nickolaou as well as the censure of Ms. Lombardi.

Mr. Nickolaou and Ms. Lombardi sought review of the CBOE's disciplinary action before the Commission pursuant to Section 19(d) of the Securities Exchange Act, 15 U.S.C. 78s(d). The Commission, after considering briefs filed by petitioners and the CBOE and hearing oral argument, issued the order here under review affirming the CBOE's disciplinary action against the petitioners, subject to modification of the sanctions imposed on Mr. Nickolaou. The Commission utilized a "clear and convincing" standard of proof to find that petitioners had engaged in a scheme to depress the market price of IBM stock, stating that the motive for the scheme was clear: Having built a substantial short position in IBM call options, if Mr. Nickolaou succeeded in lowering the price of IBM stock, he stood to gain a substantial profit and avert a possible loss by immediately covering his short position. Based on Ms. Lombardi's friendship with Mr. Nickolaou and her access to bland order tickets and the information necessary to fill them out, and to the pneumatic tube system that carried the order tickets to the Merrill Lynch wire room, the Commission found the inference convincing that she assisted Mr. Nickolaou in carrying out his manipulative scheme. The Commission further found that the CBOE was justified in accepting the handwriting expert's testimony that the same person who executed all of the exemplars had also executed the fictitious IBM tickets. The Commission reduced the sanction imposed on Mr. Nickolaou by the CBOE Board of Directors, reinstating the three-year suspension from Exchange membership and association with any Exchange member imposed by the Business Conduct Committee, and then affirmed the remaining sanctions imposed on petitioners as not excessive or oppressive.

The issues that are of a significant nature are (1) whether the Commission's order is supported by sub-

stantial evidence, and (2) whether petitioners should be allowed to submit additional evidence before the Commission upon remand.

I—SUBSTANTIAL EVIDENCE

The standard this court must apply to review of findings of fact of the Commission is that if they are supported by substantial evidence, the findings are conclusive. 15 U.S.C. § 78y(a)(4); *see Shultz* v. *Securities and Exchange Com'n.*, 614 F.2d 561 (7th Cir. 1980). We are convinced that there is substantial evidence in the record to support the conclusion that Mr. Nickolaou has violated CBOE rules. The uncontradicted testimony of the handwriting expert, itself, is substantial evidence to support a finding that Mr. Nickolaou wrote the three fictitious orders to sell the 37,500 shares of IBM stock. We are convinced that a motive did exist for placing the fictitious orders—they would have possibly driven down the price of IBM stock and, therefore, the price of IBM options and Mr. Nickolaou would have offset the options he had written which still had several weeks to run. A rise in the price of IBM stock above the option exercise price would potentially cause holders to exercise their options and, if the stock rose sufficiently, Mr. Nickolaou's loss could even exceed his premiums. The fact that the fictitious orders here involved were never executed and that similar large sales had not decreased the market price is irrelevant. The potential to affect the market in such a manner as to reduce Mr. Nickolaou's loss is sufficient.

With respect to Ms. Lombardi, once it is clear that the orders had been written by Mr. Nickolaou and that he had no business connection with Merrill Lynch, a reasonable conclusion is that he had help from an insider. Mr. Nickolaou's friendship with Ms. Lombardi was well known and is not contested. The account information used on the fictitious order tickets was information to which Ms. Lombardi had daily access. Finally, there is evidence which places Ms. Lombardi near the pneumatic tube at

the approximate time the fictitious orders were transferred to the wire room. The Commission's inference that Ms. Lombardi assisted in preparing and delivering the fictitious order tickets is reasonable and is drawn from substantial evidence in the record.

The parties to this petition have disputed the burden of proof required of the CBOE and of the Commission in this proceeding. We hold that because the Supreme Court has granted certiorari in *Steadman* v. *Securities and Exchange Commission,* 603 F.2d 1126 (5th Cir. 1978), *cert. granted* 48 U.S.L.W. 3698 (April 28, 1980), we need not examine this question in light of the fact that the Commission has independently examined the record and concluded that by clear and convincing evidence petitioners have violated CBOE rules.

II—LEAVE TO ADDUCE ADDITIONAL EVIDENCE

Petitioners have moved for leave to adduce additional evidence as permitted under Section 25(c)(1) of the Securities Exchange Act, 15 U.S.C. § 78y(c)(1), which provides in part:

> If either party applies to the court for leave to adduce additional evidence and shows to the satisfaction of the court that the additional evidence is material and that there was reasonable ground for failure to adduce it before the Commission, the court may remand the case to the Commission for further proceedings, in whatever manner and on whatever conditions the court considers appropriate.

This court is not satisfied that there was reasonable ground for failure to adduce any such "additional evidence" before either the Business Conduct Committee of the CBOE or before the Commission. The record is clear that petitioners refused to testify before the Business Conduct Committee and could have but did not move for leave to testify and adduce evidence before the Commission. Petitioners' affidavits which make vague reference to a possible report by Merrill Lynch which allegedly in-

dicates that employees other than petitioners may have been involved is too speculative. Even if such a report exists, petitioners have failed to persuade this court that such evidence could not have been adduced at an earlier stage in this proceeding. Petitioners' motion for leave to adduce additional evidence is DENIED.

Finally, we briefly note that petitioners' challenge to procedural matters concerning the CBOE proceedings is not properly before this court, in that objections were not raised before the Commission. 15 U.S.C. § 78y(c)(1). In any event, we are convinced that the alleged errors on the part of the CBOE have not lead to errors on the part of the Commission and therefore we will not give further consideration to these allegations. *Shultz, supra* at 568.

The order of the Commission is AFFIRMED.

Unpublished Per Curiam Order

JUDGMENT—ORAL ARGUMENT

UNITED STATES COURT OF APPEALS

For the Seventh Circuit

Chicago, Illinois 60604

July 18, 1980

Before

Hon. THOMAS E. FAIRCHILD, *Chief Judge*
Hon. WALTER J. CUMMINGS, *Circuit Judge*
Hon. ROBERT A. GRANT, *Senior District Judge**

No. 79-2314

NICHOLAS J. NICKOLAOU and AUDREY LOMBARDI,

Petitioners,

vs.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

Petition for Review of an Order of the Securities and Exchange Commission.

This cause was heard on the record from the Securities and Exchange Commission, and was argued by counsel.

On consideration whereof, it is ordered and adjudged by this Court that the order of the Commission in this cause appealed from be, and the same is hereby, AFFIRMED, with costs, in accordance with the order of this court filed this date.

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* Senior District Judge Robert A. Grant of the Northern District of Indiana is sitting by designation.

Unpublished Per Curiam Order

AMENDED JUDGMENT ORDER

UNITED STATES COURT OF APPEALS

For the Seventh Circuit

Chicago, Illinois 60604

Amended August 12, 1980

July 18, 1980

Before

Hon. THOMAS E. FAIRCHILD, *Chief Judge*
Hon. WALTER J. CUMMINGS, *Circuit Judge*
Hon. ROBERT A. GRANT, *Senior District Judge**

No. 79-2314

NICHOLAS J. NICKOLAOU and AUDREY LOMBARDI,

Petitioners,

vs.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

Petition for Review of an Order of the Securities and Exchange Commission.

This cause was heard on the record from the Securities and Exchange Commission, and was argued by counsel.

On consideration whereof, it is ordered and adjudged by this Court that the order of the Commission in this cause appealed from be, and the same is hereby, AFFIRMED, in accordance with the order of this Court entered this date.

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* Senior District Judge Robert A. Grant of the Northern District of Indiana is sitting by designation.

SECURITIES AND EXCHANGE COMMISSION

Washington, D. C.

SECURITIES EXCHANGE ACT OF 1934

Rel. No. 16210/September 18, 1979
Admin. Proc. File No. 3-5542
In the Matter of the Application of
NICHOLAS J. NICKOLAOU
5850 West 87th Street
Burbank, Illinois
and
AUDREY LOMBARDI
2450 West 71st Street
Chicago, Illinois

For Review of Disciplinary Action Taken by the
CHICAGO BOARD OPTIONS EXCHANGE, INC.

OPINION OF THE COMMISSION

NATIONAL SECURITIES EXCHANGE—REVIEW OF DISCIPLINARY PROCEEDINGS

Violations of Rules Governing Business Conduct
Attempt to Manipulate Market

Where exchange market maker and employee of member firm attempted to depress market price of security by submitting fictitious sale orders for execution on the New York Stock Exchange, exchange's finding of attemped manipulation *sustained,* but sanctions imposed on market maker *reduced,* since exchange had improperly increased them without notice to market maker when he appealed from decision of exchange's business conduct committee.

APPEARANCES:

Arthur M. Gorov and *Norman N. Berkson,* of Berkson, Gorov & Levin, Ltd., for Nicholas J. Nickolaou and Audrey Lombardi.
Arne R. Rode, for the Chicago Board Options Exchange, Inc.

I.

Nicholas J. Nickolaou, a market maker on the Chicago Board Options Exchange, Inc. ("CBOE") specializing in IBM option contracts, and Audrey Lombardi, an employee in the Chicago office of Merrill, Lynch, Pierce, Fenner, & Smith, a CBOE member firm, appeal from CBOE disciplinary action. The Exchange found that applicants engaged in a manipulative scheme to depress the market price of IBM on the New York Stock Exchange ("NYSE") so that Nickolaou could profit from his short position in IBM call options. Specifically, the CBOE found that Nickolaou wrote three fictitous IBM sale orders and, with Lombardi's assistance, sought to have them delivered to the NYSE for execution. The Exchange censured Nickolaou, fined him $10,000, expelled him from membership, and barred him from association with any CBOE member. Lombardi was censured.[1] On the basis of an independent review of the record, we make the following findings.[2]

II.

Within a ten minute period on the morning of March 30, 1977, Merrill Lynch's Chicago wire room[3] received three tickets ordering the sale of a total of 37,500 shares of IBM common stock at market on the NYSE. The order tickets were delivered to the wire room by means of a pneumatic tube connecting the wire room with Merrill Lynch's institutional department. A wire room employee

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[1] We stayed Nickolaou's sanctions to the extent that they would require him to sell his CBOE membership. Lombardi was granted a stay of the censure imposed on her.

[2] Assuming, without deciding, that a clear and convincing standard of proof is applicable to these proceedings, we find that the evidence meets that standard.

[3] The wire room transmits orders to New York for execution.

questioned the authenticity of the tickets because the handwriting on them did not appear to be that of the designated account executive, the specified share amounts were punctuated with periods rather than commas (e.g. 12.000, rather than 12,000), and because institutional orders were usually executed by telephone. An immediate investigation disclosed that the account executive in question did not write the tickets, and neither he nor the purported customer knew anything about them. Accordingly, Merrill Lynch did not execute the orders.

On three consecutive trading days ending March 30, 1977, Nickolaou had acquired a substantial short position in IBM call options expiring in April.[4] By March 30, he was short 107 options, each of which gave the holder the right to purchase 100 shares of IBM at $280 per share. On that day, the options were at or near their striking price, with the price of IBM common stock on the NYSE ranging from 275¾ to 280½.

The testimony of a handwriting expert[5] clearly establishes that Nickolaou filled out the fictitious order tickets. Comparing the handprinting on the order tickets with about 35 of Nickolaou's market maker trading cards (which he had admittedly written), with Nickolaou's CBOE membership application (which he had admittedly filled out), and with other materials in Nickolaou's CBOE membership file, the expert concluded that the same person had executed *all* of the documents.

During the relevant period, Lombardi was a sales assistant in Merrill Lynch's institutional department. She was a friend of Nickolaou, and he frequently visited her at Merrill Lynch's office.[6] In her capacity as sales assistant, Lombardi knew how to fill out and route order tickets. She also had access to the type of information,

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[4] The CBOE erroneously referred to these options as having July expiration dates.

[5] Respondents stipulated to this witness's expertise.

[6] In January 1977, Nickolaou designated Lombardi as his employee in a CBOE floor badge application.

such as account numbers and the numbers of account executives, that was necessary to write up the IBM orders in question. Her desk was located only about 10 feet from the pneumatic tube that carried those orders to the Merrill Lynch wire room. Lombardi was at work on the morning of March 30, and, together with other institutional department employees, was questioned about the fictitious order tickets shortly after it was discovered that they were not authentic.

We conclude, as did the CBOE, that Nickolaou, in concert with Lombardi, engaged in a manipulative scheme to depress the market price of IBM stock. The motive for the scheme is clear. Immediately prior to and including March 30, Nickolaou had built up a substantial short position in IBM call options. If he succeeded in lowering the price of IBM, he stood to gain a substantial profit, and avert a possible loss, by immediately covering his short position.

Nickolaou's handprinting appears on the fictitious order tickets. Lombardi, Nickolaou's friend, had access to blank ticket forms, to the information necessary to fill them out, and to the pneumatic tube that carried the executed tickets to the Merrill Lynch wire room. We think the inference convincing that she assisted Nickolaou in carrying out his manipulative scheme.

In addition, like the CBOE, we consider that an adverse inference may properly be drawn against applicants because of their failure to testify.[7]

We accordingly affirm the CBOE's findings of violation.

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[7] See *Baxter* v. *Palmigiano,* 425 U.S. 308, 316-320 (1976); *Lefkowitz* v. *Cunningham,* 431 U.S. 801, 808, n. 5 (1977); *Arthurs* v. *Stern,* 560 F.2d 477, 478 (C.A. 1, 1977), *cert. denied,* 434 U.S. 1034 (1978). See also *S.E.C.* v. *Gilbert,* 79 F.R.D. 683, 685-686 (S.D.N.Y., 1978).

III.

Applicants admit that the testimony of the handwriting expert "would seem to be extremely damaging to Nickolaou and through him to Lombardi." However, they argue that the testimony should have been stricken because it was based on a comparison of the fictitous order tickets with documents that had not been authenticated as having been written by Nickolaou.

This contention is without merit. The documents to which the handwriting expert compared the order tickets consisted of Nickolaou's CBOE membership application; about 35 market maker trading cards bearing, among other things, Nickolaou's initials and account number; and certain other documents that were taken from Nickolaou's CBOE membership file. Applicants stipulated that Nickolaou had filled out the membership application; that the market maker trading cards were authentic; and that two other documents, Nickolaou's floor broker and market maker applications, had "apparently" been filled out by Nickolaou.[8] The handwriting expert testified that he had initially examined all of the handwriting exemplars and determined that *one person* had executed *all* of them. In light of that testimony, and applicants' stipulations that Nickolaou had executed *some* of the "known" documents, the CBOE was justified in concluding that Nickolaou had executed all of those documents.[9] Accordingly, the Exchange was also justified in accepting the expert's further testimony that the same person who had executed the "known" exemplars had also executed the fictitious IBM order tickets.

Applicants further argue that it is improper to draw an adverse inference from their failure to testify. They as-

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[8] Applicants refused to stipulate to the authenticity of Nickolaou's application for broker-dealer registration because the CBOE only had a photocopy of the original filed with us in Washington.

[9] Thus, contrary to applicants' contention, the documents were properly admitted into evidence.

sert that the CBOE failed to prove a *prima facie* case against them, a necessary prerequisite to drawing such an inference; that they cannot be accused of "standing mute," since they denied the charges against them, under oath, in their formal answers to the CBOE's complaint; and that having moved for a directed verdict at the close of the CBOE's case, they could not have proceeded to introduce any evidence since to do so would have constituted a waiver of their motion under Illinois law.[10]

These arguments are without merit. The evidence adduced was clearly sufficient to warrant the drawing of an adverse inference from applicants' failure to testify. And applicants' formal denial of mere allegations was not the same as remaining silent in the face of the evidence adduced against them, nor an adequate substitute for taking the stand and subjecting themselves to cross-examination.[11] It would not appear that the procedural law of Illinois is applicable to proceedings before the CBOE.[12] But, even assuming that it were, it has been held that an adverse inference is not precluded where respondents are put to a choice such as the one applicants had to make here.[13] In any event, it appears that applicants waived their motion for a directed verdict by introducing evidence after their motion was denied.[14]

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[10] See *People* v. *Washington,* 23 Ill. 2d 546, 179 N.E. 2d 635, 636 (1962).

[11] See *Local 167, International Brotherhood of Teamsters* v. *U.S.,* 291 U.S. 293, 298 (1934).

[12] See *Local 167, International Brotherhood of Team-*134, 142-143 (1940); 1 Davis, Administrative Law § 803 (1958).

[13] See *Arthurs* v. *Stern, supra,* 560 F.2d at 478-479.

[14] See *People* v. *Washington, supra.* The evidence introduced by applicants consisted of certain trading records of Nickolaou.
Applicants also contend that any finding that Lombardi was in her office shortly after the fictitous or-

IV.

Applicants raise various procedural contentions. They argue that the Business Conduct Committee hearing panel should have disqualified itself because, prior to the hearing, it was furnished by the CBOE staff with copies of all of the staff's proposed exhibits, some of which were prejudicial and later excluded from evidence. They further contend that a member of the CBOE's prosecutorial staff improperly served as counsel to the panel and participated in its deliberations.

We cannot agree that any improprieties occurred. The CBOE's rules specifically provide that the hearing panel, which is required to determine all questions concerning the admissibility of evidence,[15] must be furnished in advance with all documents that the parties intend to introduce at the hearings.[16] Applicants were specifically advised by the panel that only those documents that were accepted into evidence would be considered in the disposition of applicants' case, and there is nothing in the record to indicate the contrary.[17]

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[14] (Continued)

ders were discovered can only be based on "the rankest of hearsay." In fact, our finding to that effect is based on deposition testimony that was introduced into evidence pursuant to the stipulation of the parties. The record does not support applicants' further claim that their "alleged expertise in completing market order tickets" would have made them aware that the fictitious IBM orders would be questioned and stopped.

[15] Rule 17.5(c).

[16] Rule 17.5(b).

[17] Cf. *Withrow* v. *Larkin*, 421 U.S. 35, 55 (1975): "The mere exposure to evidence presented in nonadversary investigative procedures is insufficient in itself to impugn the fairness of the Board members at a later adversary hearing."

We also note that the Conduct Committee's decision was accorded *de novo* review by both the CBOE's Board of Directors and by this Commission. See *R. H. Johnson & Co.* v. *S.E.C.*, 198 F.2d 690, 695 (C.A. 2, 1952), *cert. denied*, 344 U.S. 855.

There is also no evidence that counsel to the hearing panel played any role in the investigation or prosecution of this case. And counsel has specifically denied that allegation. Moreover, the hearing panel's chairman explicitly stated that counsel merely assisted the panel by answering questions about CBOE rules and similar matters, and did not participate in the panel's deliberations.

V.

The CBOE's Board of Directors, while affirming the censure and $10,000 fine imposed on Nickolaou by the Business Conduct Committee, increased to an expulsion and bar the Committee's assessment of three-year suspensions from Exchange membership and from association with any Exchange member. Nickolaou complains that the Board's action did not comply with Exchange rules. We agree.

In this case, Nickolaou and Lombardi requested the CBOE Board to review the decision of the Business Conduct Committee. Rule 17.9(b) of the CBOE's rules, as then in effect, provided, with exceptions not relevant here, that such review would be based "solely upon the record and the written exceptions filed by the parties." The CBOE's staff did not file any exceptions to the Committee's decision and, although it had the power to do so,[18] the Board did not order review of applicants' case on its own motion. Thus Nickolaou was not given any notice that the Board might increase the sanctions imposed on him, and had no opportunity to present evidence or argument on that issue.

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[18] Rule 17.9(c).

Under the circumstances, we conclude that the Board's increase of Nickolaou's sanctions was improper.[19] In view of the seriousness of Nickolaou's misconduct, however, we further conclude that the sanctions imposed on him by the Business Conduct Committee are appropriate in the public interest, and we shall accordingly reinstate those sanctions. The light sanction assessed against Lombardi because of her subordinate role is clearly not excessive or oppressive.

An appropriate order will issue.

By the Commission (Commissioners LOOMIS, EVANS, POLLACK and KARMEL); Chairman WILLIAMS not participating.

George A. Fitzsimmons
Secretary

/s/ Shirley E. Hollis
By: Shirley E. Hollis
Assistant Secretary

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[19] See *Todd & Co., Inc.* v. *S.E.C.*, 557 F.2d 1008, 1014 (C.A. 3, 1977).

UNITED STATES OF AMERICA

before the

SECURITIES AND EXCHANGE COMMISSION
SECURITIES EXCHANGE ACT OF 1934
Rel. No. 16210/Septemer 18, 1979
In the Matter of the Application of
NICHOLAS J. NICKOLAOU
5850 West 87th Street
Burbank, Illinois
and
AUDREY LOMBARDI
2450 West 71st Street
Chicago, Illinois

For Review of Disciplinary Action Taken by the
CHICAGO BOARD OPTIONS EXCHANGE, INC.
ORDER AFFIRMING IN PART AND MODIFYING IN PART DISCIPLINARY ACTION TAKEN BY NATIONAL SECURITIES EXCHANGE

On the basis of the Commission opinion issued this day, it is

ORDERED that the fine and censure imposed by the Chicago Board Options Exchange, Inc. on Nicholas J. Nickolaou, and the censure imposed on Audrey Lombardi, be, and they hereby are, affirmed; and it is further

ORDERED that the Exchange's expulsion of Nickolaou from membership, and its bar of Nickolaou from association with any Exchange member, be, and they hereby are, reduced to three-year suspensions from membership and from any such association.

George A. Fitzsimmons
Secretary

/s/ Shirley E. Hollis
By: Shirley E. Hollis
Assistant Secretary

No. 80-655

In the Supreme Court of the United States

OCTOBER TERM, 1980

NICHOLAS J. NICKOLAOU AND AUDREY LOMBARDI,
PETITIONERS

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

MEMORANDUM FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

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Petitioners claim (Pet. 3) that the Chicago Board Options Exchange and the Securities and Exchange Commission imposed sanctions against them without applying a "clear and convincing evidence" standard of proof.

Petitioners were sanctioned by the Chicago Board Options Exchange (CBOE) for violations of certain CBOE rules, based on their attempts to manipulate the market price of IBM stock and options. The evidence at their hearing established that they forged three large orders to sell stock and delivered those orders for execution (Pet. App. 2a-4a). Following an independent review of the record of the CBOE disciplinary proceeding under Section 19(e) of the Securities Exchange Act of 1934, 15 U.S.C. 78s(e), the Commission found, based on

its application of the "clear and convincing evidence" standard of proof, that petitioners had violated the CBOE rules (Pet. App. 12a n.2).[1]

On review of the Commission's order under Section 25(a) of the Securities Exchange Act of 1934, 15 U.S.C. 78y(a), the court of appeals found substantial evidence to support the Commission's factual findings (Pet. App. 6a). The court did not consider the question whether a "clear and convincing evidence" standard should have been used by the CBOE "in light of the fact that the Commission has independently examined the record and concluded that by clear and convincing evidence petitioners have violated CBOE rules" (*id.* at 7a).

Contrary to petitioners' assertion (Pet. 3), this case and *Steadman* v. *SEC*, 603 F. 2d 1126 (5th Cir. 1979), cert. granted, No. 79-1266 (Apr. 28, 1980), are not "companion" cases. Moreover, in contrast to *Steadman,* the Commission, in an abundance of caution, utilized the "clear and convincing evidence" standard of proof to evaluate the record in this proceeding.[2] Accordingly, there is no need to hold the present petition pending disposition of the *Steadman* case.[3]

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[1] The Commission assumed, without deciding, that the "clear and convincing evidence" standard of proof is applicable in this proceeding (Pet. App. 12a n.2). The Commission modified one portion of the sanction imposed on petitioner Nickolaou, but otherwise affirmed the sanctions ordered by the CBOE (*id.* at 18a-19a).

[2] In affirming a disciplinary order entered by a self-regulatory organization, the Commission must make its own independent finding of a violation. *Shultz* v. *SEC*, 614 F. 2d 561, 568 (7th Cir. 1980); *Sartain* v. *SEC*, 601 F. 2d 1366, 1371 (9th Cir. 1979); *Todd & Co.* v. *SEC*, 557 F. 2d 1008, 1012 (3d Cir. 1977); *R. H. Johnson & Co.* v. *SEC*, 198 F. 2d 690, 695 (2d Cir.), cert. denied, 344 U.S. 855 (1952).

[3] We also note that the petition was not filed within the 90 day period prescribed under 28 U.S.C. 2101(c). The judgment of the court

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

WADE H. MCCREE, JR.
Solicitor General

RALPH C. FERRARA
General Counsel
Securities and Exchange Commission

NOVEMBER 1980

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of appeals in this civil case was entered on July 18, 1980 (Pet. App. 9a). Petitioners did not seek rehearing, nor did they obtain an extension of time for filing a petition for a writ of certiorari. Accordingly, the 90 day period prescribed by Section 2101(c) expired on October 16, 1980. The petition was not received by the Court until October 17, 1980.

At the Commission's request, the court of appeals amended its judgment on August 12, 1980, to delete an award of costs in the Commission's favor that was not authorized by statute (Pet. App. 10a). The Commission's request to delete the erroneous award of costs did not stay the running of the period of time in which to petition for certiorari because the amended judgment did not change a matter of substance in the judgment previously rendered. *FTC* v. *Minneapolis-Honeywell Regulator Co.*, 344 U.S. 206, 211 (1952).

We are advised that petitioner has not filed a notarized statement from a member of the bar of this Court setting forth the information required by Rule 28.2 of the Rules of the Court, which is necessary if petitioner wishes to rely on the date of mailing of the petition rather than the date of actual receipt by the Clerk's office.

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